

TESSCO TECHNOLOGIES INC  
Form 10-Q  
February 11, 2009  
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## UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

## FORM 10-Q

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended December 28, 2008

or

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 0-24746

## ***TESSCO TECHNOLOGIES INCORPORATED***

(Exact name of registrant as specified in its charter)

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**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**52-0729657**  
(I.R.S Employer  
Identification No.)

**11126 McCormick Road, Hunt Valley, Maryland**  
(Address of principal executive offices)

**21031**  
(Zip Code)

**(410) 229-1000**

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.  
Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

The number of shares of the registrant's Common Stock, \$0.01 par value per share, outstanding as of January 30, 2009, was 4,688,831.

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**Table of Contents****PART I. FINANCIAL INFORMATION****Item 1. Financial Statements.****TESSCO TECHNOLOGIES INCORPORATED****Consolidated Balance Sheets**

	<b>December 28, 2008 (unaudited)</b>	<b>March 30, 2008</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 1,433,200	\$ 2,086,200
Trade accounts receivable, net	44,823,500	55,698,600
Product inventory, net	51,663,100	49,057,300
Deferred tax assets	4,048,800	4,048,800
Prepaid expenses and other current assets	3,361,600	1,827,500
Total current assets	105,330,200	112,718,400
Property and equipment, net	21,662,200	22,233,600
Goodwill, net	6,550,700	6,310,100
Other long-term assets	2,252,500	2,536,500
Total assets	\$ 135,795,600	\$ 143,798,600
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Trade accounts payable	\$ 51,515,600	\$ 64,433,400
Payroll, benefits and taxes	6,460,400	3,014,400
Income and sales tax liabilities	3,666,800	3,588,700
Accrued expenses and other current liabilities	1,343,000	1,253,600
Revolving line of credit	6,182,600	3,353,500
Current portion of long-term debt	361,400	360,400
Total current liabilities	69,529,800	76,004,000
Deferred tax liabilities	2,189,300	2,189,300
Long-term debt, net of current portion	3,572,100	3,842,600
Other long-term liabilities	1,471,700	1,611,100
Total liabilities	76,762,900	83,647,000
Shareholders' equity:		
Preferred stock		
Common stock	79,700	78,200
Additional paid-in capital	33,885,400	32,087,400
Treasury stock	(41,873,900)	(33,454,300)
Retained earnings	67,095,700	61,552,900
Accumulated other comprehensive loss, net of tax	(154,200)	(112,600)

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Total shareholders' equity		59,032,700		60,151,600
Total liabilities and shareholders' equity	\$	135,795,600	\$	143,798,600

See accompanying notes.

Table of Contents**TESSCO TECHNOLOGIES INCORPORATED****Consolidated Statements of Income**

	Fiscal Quarters Ended		Nine Months Ended	
	December 28, 2008 (unaudited)	December 30, 2007 (unaudited)	December 28, 2008 (unaudited)	December 30, 2007 (unaudited)
Revenues	\$ 118,943,300	\$ 135,732,000	\$ 384,785,300	\$ 392,680,400
Cost of goods sold	89,675,900	105,329,600	290,284,400	305,436,400
Gross profit	29,267,400	30,402,400	94,500,900	87,244,000
Selling, general and administrative expenses	26,868,200	27,729,000	84,660,800	81,737,800
Income from operations	2,399,200	2,673,400	9,840,100	5,506,200
Interest expense, net	213,700	161,000	516,400	337,800
Income before provision for income taxes	2,185,500	2,512,400	9,323,700	5,168,400
Provision for income taxes	944,100	978,100	3,780,900	2,051,700
Net income	\$ 1,241,400	\$ 1,534,300	\$ 5,542,800	\$ 3,116,700
Basic earnings per share	\$ 0.26	\$ 0.30	\$ 1.12	\$ 0.59
Diluted earnings per share	\$ 0.25	\$ 0.29	\$ 1.09	\$ 0.56
Basic weighted average shares outstanding	4,743,300	5,151,800	4,944,800	5,299,400
Diluted weighted average shares outstanding	4,871,900	5,374,400	5,085,100	5,535,800

See accompanying notes.

Table of Contents**TESSCO TECHNOLOGIES INCORPORATED****Consolidated Statements of Cash Flows**

	Nine Months Ended	
	December 28, 2008 (unaudited)	December 30, 2007 (unaudited)
Cash flows from operating activities:		
Net income	\$ 5,542,800	\$ 3,116,700
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	3,164,900	3,637,400
Gain on sale of property and equipment	(157,600)	
Non-cash stock compensation expense	1,350,500	1,514,400
Deferred income taxes and other	(61,800)	68,700
Change in trade accounts receivable	10,875,100	(7,085,200)
Change in product inventory	(2,605,800)	(17,021,700)
Change in prepaid expenses and other current assets	(755,800)	(302,200)
Change in trade accounts payable	(11,849,400)	19,982,700
Change in payroll, benefits and taxes	3,446,000	(3,199,500)
Change in income and sales tax liabilities	(700,200)	(353,600)
Change in accrued expenses and other current liabilities	291,800	115,100
Net cash provided by operating activities	8,540,500	472,800
Cash flows from investing activities:		
Purchases of property and equipment	(2,491,100)	(2,282,900)
Proceeds from sale of property and equipment	220,000	
Acquisition of business in purchase transaction and additional earn-out payments on acquired businesses	(1,309,000)	(2,330,000)
Net cash used in investing activities	(3,580,100)	(4,612,900)
Cash flows from financing activities:		
Net borrowings on revolving line of credit	2,829,100	6,059,000
Payments on long-term debt	(269,500)	(266,800)
Proceeds from issuance of stock	58,700	563,900
Purchases of treasury stock	(8,419,600)	(6,238,100)
Excess tax benefit from stock-based compensation	187,900	1,134,000
Net cash (used in) provided by financing activities	(5,613,400)	1,252,000
Net decrease in cash and cash equivalents	(653,000)	(2,888,100)
Cash and cash equivalents, beginning of period	2,086,200	4,176,300
Cash and cash equivalents, end of period	\$ 1,433,200	\$ 1,288,200

See accompanying notes.

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**TESSCO TECHNOLOGIES INCORPORATED**

**Notes to Consolidated Financial Statements**

**December 28, 2008**

(Unaudited)

***Note 1. Description of Business and Basis of Presentation***

TESSCO Technologies Incorporated, a Delaware corporation (TESSCO or the Company), is a leading provider of integrated product and supply chain solutions to the professionals that design, build, run, maintain and use wireless, mobile, fixed and in-building systems. The Company provides marketing and sales services, knowledge and supply chain management, product-solution delivery and control systems utilizing extensive Internet and information technology. Approximately 95% of the Company's sales are made to customers in the United States. The Company takes orders in several ways, including phone, fax, online and through electronic data interchange.

In management's opinion, the accompanying interim financial statements of the Company include all adjustments, consisting only of normal, recurring adjustments, necessary for a fair presentation of the Company's financial position for the interim periods presented. These statements are presented in accordance with the rules and regulations of the United States Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in the Company's annual financial statements have been omitted from these statements, as permitted under the applicable rules and regulations. The results of operations presented in the accompanying interim financial statements are not necessarily representative of operations for an entire year. The information included in this Form 10-Q should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended March 30, 2008.

***Note 2. Recently Issued Accounting Pronouncements***

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 157, Fair Value Measurements, which provides guidance for using fair value to measure assets and liabilities. The standard also responds to investors requests for expanded information about the extent to which companies measure assets and liabilities at fair value, the information used to measure fair value, and the effect of fair value measurements on earnings. The standard applies whenever other standards require (or permit) assets or liabilities to be measured at fair value. The standard does not expand the use of fair value in any new circumstances. In February 2008, the FASB partially deferred the effective date of SFAS No. 157 for certain non-financial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis until fiscal years beginning after November 15, 2008 or in the Company's case, the fiscal year beginning March 30, 2009. The Company adopted SFAS No. 157 for its financial assets and liabilities effective as of March 31, 2008, and has elected to defer its adoption for non-financial assets and liabilities until fiscal year 2010. The adoption of SFAS No. 157 did not have a material impact on the Company's consolidated financial statements (see Note 4).

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115. SFAS No. 159 permits an entity to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. Entities that elect the fair value option will report unrealized gains and losses in earnings at each subsequent reporting date. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. The Company



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adopted SFAS No. 159 effective as of March 31, 2008. As the Company did not elect to apply the fair value option as described under SFAS No. 159 to any of its financial assets or liabilities which were not currently required to be measured at fair value, the adoption of SFAS No. 159 did not have an impact on the Company's financial statements.

In December 2007, the FASB issued SFAS No. 141(R), Business Combinations, which replaces SFAS No. 141. The standard retains the fundamental requirements of SFAS No. 141 that the acquisition method of accounting (labeled the purchase method under SFAS No. 141) be used for all business combinations and that an acquirer be identified for each business combination. SFAS No. 141(R) requires the assets, liabilities, noncontrolling interests, certain acquired contingencies and contingent consideration acquired during a business combination to be measured at their fair value as of the acquisition date. SFAS No. 141(R) is effective for fiscal years beginning on or after December 15, 2008. The Company will adopt SFAS No. 141(R) on March 30, 2009.

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In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities* an amendment of FASB Statement No. 133. Under SFAS No. 161, entities are required to provide enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under FASB Statement No. 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance and cash flows. The provisions of this statement are effective for periods beginning after November 15, 2008, and both early application and comparative disclosures are encouraged. The Company is currently reviewing SFAS No. 161 to determine the impact of adoption on its financial statements.

In May 2008, the FASB issued SFAS No. 162, *The Hierarchy of Generally Accepted Accounting Principles*. This standard identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles. SFAS No. 162 directs the hierarchy to the entity, rather than the auditors, as the entity is responsible for selecting accounting principles for financial statements that are presented in conformity with generally accepted accounting principles. SFAS No. 162 is effective 60 days following the SEC's September 16, 2008 approval of the Public Company Accounting Oversight Board (PCAOB) amendments to remove the hierarchy for accounting principles generally accepted in the United States from the PCAOB's auditing standards. The Company does not expect SFAS No. 162 to have an impact on its financial statements.

In June 2008, the FASB issued FASB Staff Position No. 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities (FSP No.03-6-1)*. FSP No. 03-6-1 requires companies to treat unvested share-based payment awards that have non-forfeitable rights to dividend or dividend equivalents as participating securities. Therefore, these financial instruments must be included in calculating basic and diluted earnings per share under the two-class method described in SFAS No. 128, *Earnings Per Share*. All prior period EPS data presented should be adjusted retrospectively upon adoption. FSP No. 03-6-1 will be effective for fiscal years beginning after December 15, 2008. Therefore, the Company is required to adopt FSP No. 03-6-1 on March 30, 2009. The Company currently has share based awards for 120,000 shares of its common stock that fall under the requirements of FSP No. 03-6-1. Although the adoption of FSP No. 03-6-1 will reduce our earnings per share, the Company does not expect the adoption to have a material impact on its basic and diluted earnings per share calculations as currently presented.

**Note 3. Stock Compensation**

The Company's selling, general and administrative expenses for the fiscal quarter and nine months ended December 28, 2008 includes \$268,600 and \$1,350,500, respectively, of non cash stock compensation expense. The Company's selling, general and administrative expenses for the fiscal quarter and nine months ended December 30, 2007 includes \$434,800 and \$1,514,400, respectively, of non cash stock compensation expense. Stock compensation expense is primarily related to our Performance Stock Unit (PSU) Program. In addition, the Company recorded an excess tax benefit directly to shareholders' equity of \$187,900 and \$1,134,000, primarily related to the PSUs which vested during the nine months ended December 28, 2008 and December 30, 2007, respectively.

**Performance Stock Units:** The following table summarizes the activity under the Company's PSU program for the first nine months of fiscal year 2009:

Nine Months Ended December 28, 2008	Weighted Average Fair Value at Grant Date
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Shares available for issue under outstanding PSUs, non-vested beginning of period	439,031	\$	16.79
Granted	275,000		11.71
Vested	(147,593)		10.42
Forfeited/cancelled	(188,020)		23.95
Shares available for issue under outstanding PSUs, non-vested end of period	378,418	\$	12.03

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Of the 378,418 shares available for issuance under outstanding PSUs but not yet vested as of December 28, 2008, 103,418 shares have been earned, and assuming the respective participants remain employed by or associated with the Company on these dates, half of these shares will vest and be issued on or about May 1 of each of 2009 and 2010.

The vast majority of the PSUs cancelled during fiscal year 2009 related to the fiscal year 2008 grant of PSUs which had a 1-year measurement period (fiscal year 2008). During that period, actual earnings per share did not reach the threshold level, and thus, those PSUs were cancelled. Per the provisions of the Second Amended and Restated 1994 Stock and Incentive Plan (the "1994 Plan"), the shares related to these PSUs were added back to the 1994 Plan and became available for future issuance.

During fiscal year 2009, the Compensation Committee of the Board of Directors, with the concurrence of the full Board of Directors, granted additional PSUs to select key individuals and directors, providing them with the opportunity to earn up to 275,000 additional shares of the Company's common stock in the aggregate, depending upon whether certain threshold or goal earnings per share targets are met, subject to individual performance for employees (independent directors are not subject to individual performance factors). These PSUs have only one measurement year (fiscal year 2009), with any shares earned at the end of fiscal year 2009 to vest and be issued 25% on or about May 1 of each of 2009, 2010, 2011 and 2012, provided that the respective participants remain employed by or associated with the Company on each such date.

If the maximum target of PSUs outstanding is assumed to be earned, total unrecognized compensation costs would be approximately \$2.4 million as of December 28, 2008 and would be expensed through fiscal year 2012.

**Stock Options:** In accordance with SFAS No. 123R, the fair value of the Company's stock options have been determined using the Black-Scholes-Merton option pricing model, based upon facts and assumptions existing at the date of grant. Stock options granted have exercise prices equal to the market price of the Company's common stock on the grant date.

The value of each option at the date of grant is amortized as compensation expense over the option service period. This occurs without regard to subsequent changes in stock price, volatility or interest rates over time, provided that the option remains outstanding. As of December 28, 2008, all outstanding stock options are fully vested. The following table summarizes the pertinent option information for outstanding options for the nine months ended December 28, 2008:

	Shares	Weighted Average Exercise Price
Outstanding, beginning of period	135,000	\$ 8.35
Granted		
Exercised		
Cancelled		
Outstanding and exercisable, end of period	135,000	8.35

**Restricted Stock:** In fiscal year 2007, the Company granted 150,000 shares of the Company's common stock to its Chairman and Chief Executive Officer as a restricted stock award under the 1994 Plan. These shares vest ratably over ten fiscal years based on service, beginning on the last day of fiscal year 2007 and ending on the last day of fiscal year 2016, subject, however, to the terms applicable to the award, including terms providing for possible acceleration of vesting upon death, disability, change in control or certain other events. The weighted average fair value for these shares at the grant date was \$15.84. No other shares of restricted stock are currently issued as awards under the 1994 Plan. As of

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December 28, 2008, 120,000 shares remain unvested and there was no activity related to these restricted shares during the third quarter of fiscal year 2009. As of December 28, 2008, there was approximately \$1.7 million of total unrecognized compensation costs related to restricted stock. Unrecognized compensation costs are expected to be recognized ratably over a period of approximately eight years.

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SFAS No. 157 requires that assets and liabilities carried at fair value be classified and disclosed in one of the following three categories:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets, and quoted prices for identical or similar assets or liabilities in markets that are not active.
- Level 3: Unobservable inputs for the asset or liability that reflect the reporting entity's own assumptions about the inputs used in pricing the asset or liability.

The following table presents information about assets and liabilities recorded at fair value on the Company's Consolidated Balance Sheet:

	Balance at December 28, 2008	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets:</b>				
Interest rate swap agreement, net of tax	\$ (154,200)	\$	\$ (154,200)	\$
Total assets at fair value	\$ (154,200)	\$	\$ (154,200)	\$

The fair value of the Company's interest rate swap agreement is included in prepaid expenses and other current assets on the Company's Consolidated Balance Sheets. The Company's fair value of its interest rate swap is derived from valuation models commonly used for derivatives. Valuation models require a variety of inputs, including contractual terms, market fixed prices, inputs from forward price yield curves, notional quantities, measures of volatility and correlations of such inputs. The Company's derivatives trade in liquid markets, and as such, model inputs can generally be verified and do not involve significant management judgment.

**Note 5. Earnings Per Share**

The dilutive effect of all options, restricted stock grants and PSUs outstanding has been determined by using the treasury stock method. The weighted average shares outstanding is calculated as follows:

Fiscal Quarters Ended		Nine Months Ended	
December 28, 2008	December 30, 2007	December 28, 2008	December 30, 2007

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Basic weighted average common shares outstanding	4,743,300	5,151,800	4,944,800	5,299,400
Effect of dilutive common stock equivalents outstanding	128,600	222,600	140,300	236,400
Diluted weighted average common shares outstanding	4,871,900	5,374,400	5,085,100	5,535,800

As of December 28, 2008, stock options with respect to 135,000 shares of common stock were outstanding. All outstanding options, restricted stock grants and earned but unvested PSUs were included in the computation of diluted earnings per share because all such instruments were dilutive.

**Note 6. Business Segments**

The Company evaluates revenue, gross profit and inventory in three business segments: (1) Network infrastructure products, which are used to build, repair and upgrade wireless telecommunications, computing and Internet networks, and generally complement radio frequency transmitting and switching equipment provided directly by original equipment manufacturers (OEMs); (2) Mobile devices and accessory products, which include data devices, pagers and two-way radios and related accessories such as replacement batteries, cases, speakers, mobile amplifiers, power supplies, headsets, mounts, car antennas and various wireless data devices; and (3) Installation, test and maintenance products, which are used to install, tune, maintain and repair wireless communications equipment. Within the mobile devices and accessories line of business, the Company sells to both commercial and consumer markets. The network infrastructure and installation, test and maintenance lines of business sell primarily to commercial markets. The Company also regularly

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reviews its results of operations in three commercial customer categories and the consumer customer category, as described further below:

- Commercial Public Carriers and Network Operators. Public carriers and network operators include systems operators that are generally responsible for building and maintaining the infrastructure system and provide airtime service to individual subscribers.
- Commercial Resellers. Resellers include dealers and resellers that sell, install and service cellular telephone, paging and two-way radio communications equipment primarily for the consumer and small business markets. These resellers include local and national proprietorships and retailers, as well as sales and installation centers operated by cellular and paging carriers.
- Commercial Self-Maintained Users and Governments. Self-maintained user (SMU) and government customers include commercial entities such as major utilities and transportation companies, federal agencies and state and local governments, including public safety organizations.
- Consumers. Consumers include customers that buy through any of our affinity partner relationships or directly from our consumer website, YourWirelessSource.comTM.

The Company measures segment performance based on segment gross profit. The segment operations develop their product offering, pricing and strategies, which are collaborative with one another and the centralized sales and marketing function. Therefore, the Company does not segregate assets, other than inventory, for internal reporting, evaluating performance or allocating capital. Product delivery revenue and certain cost of sales expenses have been allocated to each segment based on a percentage of revenues and/or gross profit, as applicable. The Company's goodwill at December 28, 2008 relates to acquisitions within its network infrastructure line of business.



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Segment activity for the third quarter of fiscal years 2009 and 2008 is as follows:

(Amounts in thousands)	Network Infrastructure	Mobile Devices and Accessories	Installation, Test and Maintenance	Total
<b><u>Fiscal Quarter ended December 28, 2008</u></b>				
Commercial Revenues:				
Public Carriers and Network Operators	\$ 11,340	\$ 535	\$ 3,073	\$ 14,948
Resellers	17,981	48,432	2,491	68,904
SMUs and Governments	14,300	3,747	14,389	32,436
Total Commercial Revenues	43,621	52,714	19,953	116,288
Consumer Revenues		2,655		2,655
Total Revenues	\$ 43,621	\$ 55,369	\$ 19,953	\$ 118,943
Commercial Gross Profit:				
Public Carriers and Network Operators	\$ 2,814	\$ 139	\$ 687	\$ 3,640
Resellers	4,906	10,973	656	16,535
SMUs and Governments	3,736	1,076	3,427	8,239
Total Commercial Gross Profit	11,456	12,188	4,770	28,414
Consumer Gross Profit		853		853
Total Gross Profit	\$ 11,456	\$ 13,041	\$ 4,770	\$ 29,267
Product Inventory	\$ 24,048	\$ 23,433	\$ 4,182	\$ 51,663
<b><u>Fiscal Quarter ended December 30, 2007</u></b>				
Commercial Revenues:				
Public Carriers and Network Operators	\$ 13,778	\$ 527	\$ 3,705	\$ 18,010
Resellers	17,084	62,975	2,318	82,377
SMUs and Governments	13,719	3,325	15,856	32,900
Total Commercial Revenues	44,581	66,827	21,879	133,287
Consumer Revenues		2,445		2,445
Total Revenues	\$ 44,581	\$ 69,272	\$ 21,879	\$ 135,732
Commercial Gross Profit:				
Public Carriers and Network Operators	\$ 3,247	\$ 147	\$ 822	\$ 4,216
Resellers	4,946	12,116	678	17,740
SMUs and Governments	3,315	973	3,260	7,548
Total Commercial Gross Profit	11,508	13,236	4,760	29,504
Consumer Gross Profit		898		898
Total Gross Profit	\$ 11,508	\$ 14,134	\$ 4,760	\$ 30,402
Product Inventory	\$ 22,256	\$ 28,138	\$ 4,077	\$ 54,471

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Segment activity for the first nine months of fiscal years 2009 and 2008 is as follows:

(Amounts in thousands)	Network Infrastructure	Mobile Devices and Accessories	Installation, Test and Maintenance	Total
<b><u>Nine Months ended December 28, 2008</u></b>				
Commercial Revenues:				
Public Carriers and Network Operators	\$ 35,545	\$ 1,655	\$ 10,133	\$ 47,333
Resellers	57,072	165,185	7,228	229,485
SMUs and Governments	41,563	11,276	46,677	99,516
Total Commercial Revenues	134,180	178,116	64,038	376,334
Consumer Revenues		8,451		8,451
Total Revenues	\$ 134,180	\$ 186,567	\$ 64,038	\$ 384,785
Commercial Gross Profit:				
Public Carriers and Network Operators	\$ 9,124	\$ 468	\$ 2,311	\$ 11,903
Resellers	15,652	37,059	1,888	54,599
SMUs and Governments	11,303	3,556	10,250	25,109
Total Commercial Gross Profit	36,079	41,083	14,449	91,611
Consumer Gross Profit		2,890		2,890
Total Gross Profit	\$ 36,079	\$ 43,973	\$ 14,449	\$ 94,501
Product Inventory	\$ 24,048	\$ 23,433	\$ 4,182	\$ 51,663
<b><u>Nine Months ended December 30, 2007</u></b>				
Commercial Revenues:				
Public Carriers and Network Operators	\$ 36,674	\$ 1,676	\$ 9,731	\$ 48,081
Resellers	52,940	180,901	6,982	240,823
SMUs and Governments	37,156	10,088	48,921	96,165
Total Commercial Revenues	126,770	192,665	65,634	385,069
Consumer Revenues		7,611		7,611
Total Revenues	\$ 126,770	\$ 200,276	\$ 65,634	\$ 392,680
Commercial Gross Profit:				
Public Carriers and Network Operators	\$ 8,725	\$ 471	\$ 2,333	\$ 11,529
Resellers	13,664	34,565	2,141	50,370
SMUs and Governments	9,349	3,137	10,048	22,534
Total Commercial Gross Profit	31,738	38,173	14,522	84,433
Consumer Gross Profit		2,811		2,811
Total Gross Profit	\$ 31,738	\$ 40,984	\$ 14,522	\$ 87,244
Product Inventory	\$ 22,256	\$ 28,138	\$ 4,077	\$ 54,471

Table of Contents**Note 7. Comprehensive Income**

The components of total comprehensive income were as follows:

	Fiscal Quarter Ended		Nine Months Ended	
	December 28, 2008	December 30, 2007	December 28, 2008	December 30, 2007
Net Income	\$ 1,241,400	\$ 1,534,300	\$ 5,542,800	\$ 3,116,700
Change in value of interest rate swap, net of tax	(101,700)	(45,100)	(41,600)	(64,800)
Total comprehensive income	\$ 1,139,700	\$ 1,489,200	\$ 5,501,200	\$ 3,051,900

**Note 8. Revolving Credit Facility and Term Loan**

During the third quarter of fiscal year 2009, the Company, and its primary operating subsidiaries, entered into a Second Modification Agreement (the Second Modification Agreement) with SunTrust Bank and Wachovia Bank, National Association, pursuant to which the Credit Agreement for the Company's existing \$50 million unsecured revolving credit facility was amended.

The Second Modification Agreement amended a negative covenant in the Credit Agreement by increasing from \$15 million to \$25 million the amount of stock permitted to be repurchased by the Company over the term of the revolving credit facility (previously increased to \$15 million by the First Modification Agreement, See Note 9). In addition, the Second Modification Agreement positively modified on a going forward basis certain other of the financial covenants applicable to the Company under the Credit Agreement, to adjust the definitions of "cash flow" and "tangible net worth" and to afford the Company limited relief from dividend restrictions.

Pursuant to the terms of the relevant documents, the financial covenants included in the Credit Agreement are also applicable to the Company's existing Term Loan with the same lenders. Accordingly, the Second Modification Agreement also had the effect of amending the terms applicable to the Term Loan.

**Note 9. Stock Buybacks**

On April 28, 2003, the Company's Board of Directors approved a stock buyback program. As of December 28, 2008, the Board of Directors has authorized the purchase of 2,395,567 shares of outstanding common stock under the stock buyback program. Shares may be purchased from time to time in the open market, by block purchase, or through negotiated transactions, or possibly other transactions managed by broker-dealers. No time limit has been set for completion or expiration of the program. As of December 28, 2008, the Company had purchased 2,281,497 shares under the stock buyback program for approximately \$30.0 million, or an average of \$13.16 per share. Of the total shares repurchased under the stock

buyback program, 140,523 shares were repurchased in the first nine months of fiscal year 2009 for approximately \$1.8 million. As of December 28, 2008, 114,070 shares remained available for repurchase under this program.

In addition to the shares repurchased in the stock buyback program discussed immediately above, on July 1, 2008 the Company repurchased all 470,000 shares of its common stock held by Brightpoint, Inc. ( Brightpoint ) in a privately negotiated transaction. Pursuant to an agreement entered into between the Company and Brightpoint, the Company purchased Brightpoint 's share holdings, comprising approximately 9% of the Company 's total then outstanding common stock, for \$13.64 per share, or a total of \$6,410,800. The price per share was determined based on the seven trading day trailing average closing price of the Company 's common stock on the NASDAQ Global Market determined as of the close of trading on June 30, 2008. The purchase price per share approximated the price of the Company 's common stock on the transaction date. The purchase was funded through available cash and borrowings under the Company 's \$50 million unsecured revolving line of credit facility. This transaction was not made under, nor does it affect the number of

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shares available for repurchase under, the Company's stock buyback program discussed above. In connection with this transaction, the Company and certain of its subsidiaries entered into a First Modification Agreement with SunTrust Bank and Wachovia Bank, National Association, to amend a negative covenant included in the Credit Agreement for the Company's existing \$50 million unsecured revolving line of credit facility, to increase the amount of common stock permitted to be repurchased by the Company (beginning on the inception date of the Credit Agreement) from \$10 million to \$15 million, during the term of the credit facility (also See Note 8 for additional modifications to the credit facility).

***Note 10. Customer Concentration***

The Company's future results could be negatively impacted by the loss of certain customer and/or vendor relationships. For the fiscal quarter and nine months ended December 28, 2008, sales of products to the Company's top customer relationship, AT&T Mobility, accounted for 20% and 23% of total revenues, respectively. For both the fiscal quarter and nine months ended December 30, 2007, sales of products to the Company's top customer relationship, AT&T Mobility, accounted for 24% and 25% of total revenues, respectively. For both the fiscal quarter and nine months ended December 28, 2008, sales of products to the Company's Nokia Inc. (Nokia) repair and replacement component relationship accounted for 7% of total revenues. For both the fiscal quarter and nine months ended December 30, 2007, sales of products to the Company's Nokia repair and replacement component relationship accounted for 8% of total revenues. The Nokia relationship is a complete supply chain relationship and, therefore, the Company has no alternative sources of supply, and the Company's purchases, and ultimately its resale of these products, is dependent upon the continuation of the Nokia relationship. As of January 2009, the Company and Nokia extended this relationship through December 2010. As part of this extension, Nokia will become the primary obligator with several of the Company's larger Nokia customers. The Company will continue to earn fees from Nokia to fulfill product to these customers, but Nokia will take on a larger role in servicing the customer. Therefore, the Company will begin to account for these sales on a net basis and will receive a smaller fee. The Company will continue to service and fulfill product to other customers and will continue to record sales to these customers on a gross basis. The Company also sells products other than Nokia repair and replacement materials to many of these customers. Absent this arrangement with Nokia, the Company would maintain the ability to sell its other products to these customers.

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**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

This commentary should be read in conjunction with the Management's Discussion and Analysis of Financial Condition and Results of Operations from the Company's Annual Report on Form 10-K for the fiscal year ended March 30, 2008.

**Business Overview and Environment**

TESSCO Technologies Incorporated (TESSCO or the Company) is a leading provider of integrated product and supply chain solutions to the professionals that design, build, run, maintain and use wireless mobile, fixed and in-building systems. Although we sell products to customers in over 100 countries, approximately 95% of our sales are made to customers in the United States. We have operations and office facilities in Hunt Valley, Maryland, Reno, Nevada and San Antonio, Texas. Due to the diversity of our business, we are not significantly affected by seasonality. However, sales to our retailers generally peak in our second and third quarters in preparation for the winter holiday season. Also, our network infrastructure sales are typically affected by weather conditions in the United States, especially in our fourth quarter.

We offer a wide range of products that are classified into three business segments: (1) network infrastructure; (2) mobile devices and accessories; and (3) installation, test and maintenance. These segments are described further below:

- **Network Infrastructure Products.** Network infrastructure products, which are sold to our commercial customers, are used to build, repair and upgrade wireless telecommunications, computing and Internet networks. Sales of traditional network infrastructure products, such as cable, transmission lines and antennas are in part dependent on capital spending in the wireless communications industry. However, we have also been growing our offering of wireless broadband and network equipment products, which are not as dependent on the overall capital spending of the industry.
- **Mobile Device and Accessory Products.** Mobile devices and accessory products include cellular phone and data device accessories, as well as two-way radios and related accessories. Mobile devices and accessory products are widely sold to commercial customers and consumers. These commercial customers include retail stores, value-added resellers and dealers, as well as self-maintained users. These consumers are primarily reached through our affinity partnerships, where we offer services including customized order fulfillment, outsourced call centers, and building and maintaining private label Internet sites. Approximately 44% of all of our mobile devices and accessory product sales for the fiscal quarter ended December 28, 2008 were generated from sales to AT&T Mobility ( AT&T ).
- **Installation, Test and Maintenance Products.** Installation, test and maintenance products, which are sold to our commercial customers, are used to install, tune, maintain and repair wireless communications equipment. Approximately 47% of all of our installation, test and maintenance sales for the fiscal quarter ended December 28,

2008 were generated from the sales of repair and replacement parts and materials for original equipment manufacturers, primarily Nokia, Inc. ( Nokia ). The remainder of this segment is made up of sophisticated analysis equipment and various frequency-, voltage- and power-measuring devices, as well as an assortment of tools, hardware and supplies required by service technicians.

Both our repair and replacement parts sales and consumer mobile devices and accessory sales through affinity partnerships, are reliant on relationships with a small number of vendors.

We regularly review four categories within each business segment: (1) commercial public carriers and network operators; (2) commercial resellers; (3) commercial self-maintained users and governments; and (4) consumers. These categories are described further below:

- Commercial Public Carriers and Network Operators. Public carriers and network operators include systems operators that are generally responsible for building and maintaining the infrastructure system and provide airtime service to individual subscribers.

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- Commercial Resellers. Resellers include dealers and resellers that sell, install and service cellular telephone, paging and two-way radio communications equipment primarily for the consumer and small business markets. These resellers include local and national proprietorships and retailers, as well as sales and installation centers operated by cellular and paging carriers.
- Commercial Self-Maintained Users (SMUs) and Governments. SMUs and government customers include commercial entities such as major utilities and transportation companies, federal agencies and state and local governments, including public safety organizations.
- Consumers. Consumers are customers buying through any of our affinity-partner relationships or directly from our consumer website, YourWirelessSource.comTM.

The wireless communications distribution industry is competitive and fragmented, and is comprised of several national distributors. In addition, many manufacturers sell direct. Barriers to entry for distributors are relatively low, particularly in the mobile devices and accessories market, and the risk of new competitors entering the market is high. Consolidation of larger wireless carriers has and will most likely continue to impact our current and potential customer base. In addition, the agreements or arrangements with our customers or vendors looking to us for product and supply chain solutions are typically of limited duration and are terminable by either party upon several months or otherwise relatively short notice. Our ability to maintain these relationships is subject to competitive pressures and challenges. We believe, however, that our strength in service, the breadth and depth of our product offering, our information technology system, and our large customer base and purchasing relationships with approximately 360 manufacturers, provides us with a significant competitive advantage over new entrants to the market.

Our third quarter revenues decreased by 12.4% compared to the third quarter of last year. This decrease was driven by a decline in each of our commercial lines of business. Gross profits increased in our installation, test and maintenance line of business as compared with the third quarter of last year. However, the increase in gross profits from our installation, test and maintenance line of business was more than offset by a decline in our network infrastructure and mobile devices and accessories lines of business. This overall decrease in gross profit, partially offset by a decrease in operating expenses, resulted in a 19.2% decline in net income and a 13.8% decrease in diluted earnings per share over the prior-year quarter.

The current global financial crisis which has included, among other things, significant reductions in available capital and liquidity from banks and other providers of credit, substantial reductions and/or fluctuations in equity and currency values worldwide, significant decreases in consumer confidence and consumer and business spending, and concerns that the worldwide economy may be in a prolonged recessionary period has adversely affected our customers' access to capital and/or willingness to spend capital on our products, and/or their levels of cash liquidity with which to pay for our products. During the third quarter, we have seen and continue to see negative impacts of the current global financial crisis, including a decline in our average number of monthly buying customers and in the average dollars purchased for each buying customer, as well as longer days to pay from our customers. We expect the economic crisis to continue to have an impact on our operating results during the fourth quarter of the fiscal year, especially in our retail and public carriers and network operators businesses. In addition, the current global financial crisis may materially adversely affect our suppliers' access to capital and liquidity, which may in turn adversely impact their ability to maintain inventories, production levels, and/or product quality, or cause them to raise prices or lower production levels, or result in their ceasing operation. The impact of the crisis on our liquidity is further discussed below under the heading Liquidity.



Table of Contents**Results of Operations**

The following table summarizes the unaudited results of our operations for the fiscal quarter and nine months ended December 28, 2008 and December 30, 2007:

(Amounts in thousands, except per share data)	Fiscal Quarters Ended				Nine Months Ended			
	December 28, 2008	December 30, 2007	\$ Change	% Change	December 28, 2008	December 30, 2007	\$ Change	% Change
<b>Commercial Revenues</b>								
<b>Network Infrastructure:</b>								
Public Carriers and Network Operators	\$ 11,340	\$ 13,778	\$ (2,438)	(17.7)%	\$ 35,545	\$ 36,674	\$ (1,129)	(3.1)%
Resellers	17,981	17,084	897	5.3%	57,072	52,940	4,132	7.8%
SMUs and Governments	14,300	13,719	581	4.2%	41,563	37,156	4,407	11.9%
<b>Total Network Infrastructure</b>	<b>43,621</b>	<b>44,581</b>	<b>(960)</b>	<b>(2.2)%</b>	<b>134,180</b>	<b>126,770</b>	<b>7,410</b>	<b>5.8%</b>
<b>Mobile Devices and Accessories:</b>								
Public Carriers and Network Operators	535	527	8	1.5%	1,655	1,676	(21)	(1.3)%
Resellers	48,432	62,975	(14,543)	(23.1)%	165,185	180,901	(15,716)	(8.7)%
SMUs and Governments	3,747	3,325	422	12.7%	11,276	10,088	1,188	11.8%
<b>Total Mobile Devices and Accessories</b>								